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No. 06-1413

Supreme Court, U.S.
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In The
Supreme Court of the United States

MEADWESTVACO CORPORATION,
successor in interest to THE MEAD CORPORATION,

Petitioner,

v.

ILLINOIS DEPARTMENT OF REVENUE, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, AND TREASURER OF THE STATE OF ILLINOIS,

Respondent.

On Petition For A Writ Of Certiorari To The Appellate Court Of Illinois

AMICUS CURIAE BRIEF IN SUPPORT OF PETITIONER, MEADWESTVACO CORPORATION, successor in interest to THE MEAD CORPORATION, SUBMITTED ON BEHALF OF GANNETT CO., INC.

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TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	ii
INTEREST OF THE *AMICUS CURIAE*	1
ARGUMENT	3
I. INTRODUCTION	3
II. AN OPERATIONAL FUNCTION SHOULD BE DETERMINED BY FOCUSING ON WHETHER THE ASSET IS OPERATIONALLY CONNECTED TO BUSINESS ACTIVITIES CONDUCTED IN THE TAXING STATE	4
A. Capital Expenditure Approval, Capital Contributions, and Cash Management Serve Financial Oversight Functions and do not Render an Out-of-State Business an Operational Function of In-State Business Activities	4
B. Segment Reporting Serves a Financial Oversight, not Operational, Function	6
III. SINCE 19 STATES SOLELY OR SIGNIFICANTLY RELY ON THIS COURT FOR THEIR DEFINITIONS OF APPORTIONABLE, "BUSINESS INCOME," THE IMPROPER AND EXPANSIVE INTERPRETATION OF OPERATIONAL FUNCTION BY THE ILLINOIS APPELLATE COURT IS AN IMPORTANT QUESTION OF FEDERAL LAW THAT SHOULD BE SETTLED BY THIS COURT	8
CONCLUSION	10

TABLE OF AUTHORITIES

Page

CASES

Allied-Signal, Inc. v. Director, Division of Taxation, 504 U.S. 768 (1992) 3, 4, 7, 9, 10

Alterman Foods, Inc. v. United States, 611 F. 2d 866 (Ct. Cl. 1979) 5

ASARCO Inc. v. Idaho State Tax Commission, 458 U.S. 307 (1982) 3

Container Corp. of America v. Franchise Tax Board, 463 U.S. 149 (1983) 3

F.W. Woolworth Co. v. Taxation & Revenue Department of New Mexico, 458 U.S. 354 (1982) 3, 6

Laidlaw Transportation, Inc. v. Commissioner, T.C. Memo 1998-232 (1998) 5

New York Times Sales, Inc. v. Commissioner of Revenue, 667 N.E. 2d 302 (Mass. Ct. App. 1996) 5

STATUTES

ALA. CODE § 40-27-1.1 9

CONN. GEN. STAT. § 12-218 9

FL. STAT. § 220.03(r) 9

GA. CODE ANN. § 48-7-31(a) 8

ILL. COMP. STAT. 5/1501(a)(1) 8

IOWA CODE § 422.32.2 9

ME. REV. STAT. ANN. tit. 36, § 5211 9

MD. CODE ANN. TAX-GEN. § 10-304 9

MASS. GEN. LAWS ch. 63, § 38 9

TABLE OF AUTHORITIES – Continued

Page

MINN. STAT. § 290.17, subd. 3 and subd. 6 8

NEB. REV. STAT. § 77-2734.06 9

N.H. REV. STAT. ANN. § 77-A:1 9

N.J. STAT. ANN. § 54:10A-6.1 9

N.C. GEN. STAT. § 105-130.4(a)(1) 8

72 PA. CONS. STAT. § 7401(3)2.(1)(a) 9

R.I. GEN. LAWS §§ 44-11-11 and 44-11-14(a) 9

VT. STAT. ANN. tit. 32, § 5811 9

VA. CODE ANN. §§ 58.1-406, 58.1-407, and 58.1-408 9

WIS. STAT. § 71.25(5)(a) 8

UNIFORM MODEL ACTS

UNIFORM DIVISION OF INCOME FOR TAX PURPOSES ACT, §§ 1(a) and (e), 7A UNIFORM LAWS ANNOTATED 141 (2005) 8

MISCELLANY

Statement of Financial Accounting Standards No. 14, *Financial Reporting for Segments of a Business Enterprise* (1976) 6, 7

Statement of Financial Accounting Standards No. 131, *Disclosures about Segments of an Enterprise and Related Information* (1997) 6, 7

INTEREST OF THE *AMICUS CURIAE*[1]

Pursuant to Rule 37.2 of the Rules of this Court, Gannett Co., Inc. ("Gannett") respectfully submits this brief as *amicus curiae* in support of Petitioner. The issues presented are of great importance to Gannett and many similarly situated companies. Gannett is the parent corporation of an affiliated group of corporations and other business entities with operations in the United States, United Kingdom, and elsewhere. Gannett is a leading international news and information company. In the United States, the company publishes 90 daily newspapers, including *USA TODAY*, and nearly 1,000 non-daily publications. The company is the largest newspaper publisher in the United States, and also operates Internet sites offering news and information customized to the market served. In addition, Gannett carries on publishing operations in the United Kingdom, operating as Newsquest, including 17 paid-for daily newspapers and almost 300 non-daily publications. Gannett's other principal business segment is its broadcasting segment that operates 23 broadcast television stations in the United States with a market reach of over 20.1 million households.

As a publicly traded corporation, Gannett must file various public documents with the Securities and Exchange Commission ("SEC"). Like all public companies, Gannett must determine its business segments and report

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[1] No counsel of a party authored this brief in whole or in part, and no person or entity, other than the *amicus curiae*, made a monetary contribution to the preparation or submission of this brief. All parties have consented to the filing of this brief, and the letters of consent of both Petitioner and Respondents have been filed with the Court pursuant to Rule 37.2(a).

these in its public financial statements filed with the SEC. Currently, Gannett has determined that its largest business segment is newspaper publishing and its other business segment is television broadcasting. Although newspaper publishing has always been Gannett's largest segment, in the past it has operated other reportable business segments, including outdoor advertising and cable television.

Like any responsible parent corporation, Gannett approves its subsidiaries' capital budgets and may contribute capital to its newspapers, television stations, and internet sites whether they are in start-up mode or mature. Likewise, Gannett maintains a cash management system to facilitate sound financial accounting controls for cash and accurate quarterly reporting of Gannett's cash position in SEC filings.

Gannett is presently involved in litigation in a number of States, including Illinois, Maine, and Montana. This litigation presents questions regarding the proper state income tax treatment of capital gains recognized by a subsidiary of Gannett that disposed of a cable television business that Gannett acquired in December 1995 as part of its acquisition of Multimedia, Inc., and held for a little over four (4) years before selling the assets to Cox Communications, Inc. in January 2000. The issue is also the subject of controversies that may be litigated in several additional States.

Gannett believes that the Illinois Appellate Court's decision below improperly interpreted this Court's operational function test in a way that effectively removes the unitary business principle as a meaningful limitation on the reach of States to tax the income of non-domiciliary

taxpayers. This is a field in which Gannett has a major interest.

ARGUMENT

I. INTRODUCTION

One of the several functions of management when serving as responsible corporate stewards for shareholders of a public company is financial oversight and transparent financial reporting. Among the common oversight roles of management are approval of capital budgets, cash management, and financial statement reporting in accordance with promulgated standards. The Illinois Appellate Court below thought these common stewardship activities caused a subsidiary corporation to serve an operational function for its parent corporation.

Since this Court's decision in *Allied-Signal, Inc. v. Director, Division of Taxation*, 504 U.S. 768 (1992), at least 19 of the 46 States and the District of Columbia that impose a corporation income tax now define and tax apportionable, business income solely or significantly in relation to the full extent permitted by the United States Constitution. This trend necessarily implicates the Court's decisions in *Allied-Signal, F.W. Woolworth Co. v. Taxation & Revenue Department of New Mexico*, 458 U.S. 354 (1982), *ASARCO Inc. v. Idaho State Tax Commission*, 458 U.S. 307 (1982), and *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159 (1983), as the only limits on State determinations of apportionable income. As a result, the improper and expansive interpretation of this Court's jurisprudence by the Illinois Appellate Court impacts the interests of Gannett and other similarly situated public

companies in a substantial number of States beyond Illinois. Petitioner's Petition for Writ of Certiorari should be granted so that the core purpose and meaning of the unitary business principle as a limitation on State taxing authority can be preserved.

II. AN OPERATIONAL FUNCTION SHOULD BE DETERMINED BY FOCUSING ON WHETHER THE ASSET IS OPERATIONALLY CONNECTED TO BUSINESS ACTIVITIES CONDUCTED IN THE TAXING STATE.

A. Capital Expenditure Approval, Capital Contributions, and Cash Management Serve Financial Oversight Functions and do not Render an Out-of-State Business an Operational Function of In-State Business Activities.

The Illinois Appellate Court's decision flaunts the purpose of the unitary business principle. The principle is a limitation on the reach of a State to tax the income or gain of a non-domiciliary taxpayer. *Allied-Signal*, 504 U.S. at 778. Thus, "... the objective characteristics of the asset's use and its relation to the taxpayer and its activities within the taxing State" is determinative of whether an asset served an operational, or investment, function. *Id.* at 785. Accordingly, whether an asset served an operational function should be determined by focusing on whether the asset is operationally connected to the business activities conducted in the taxing State. Petitioner's approval of Lexis/Nexis capital expenditures, contributions of capital, segment reporting of Lexis/Nexis in its public company financial statements, and cash management system, in addition to being common to any public company, did not, by themselves or in combination, create any

operational connection of Lexis/Nexis to Petitioner's Illinois business activities.

For example, the Illinois Appellate Court emphasized Petitioner's cash management system.[2] A cash management system is critical to a public company and promotes accounting control of cash to facilitate accurate quarterly reporting of the company's cash position in SEC filings. In addition, for tax purposes the cash advances resulting from the operation of a cash management system are normally treated as constructive dividends by the operating subsidiary to the parent corporation to the extent of the subsidiary's earnings and profits (and as a return of capital to the shareholder to the extent in excess of the subsidiary's earnings and profits). Alternatively, the cash advances may be treated as a loan if, in substance, the advances are in the nature of a loan. *Alterman Foods, Inc. v. United States*, 611 F. 2d 866 (Ct. Cl. 1979); *Laidlaw Transportation, Inc. v. Commissioner*, T.C. Memo. 1998-232 (1998); *New York Times Sales, Inc. v. Commissioner of Revenue*, 667 N.E. 2d 302 (Mass. Ct. App. 1996). Thus, when properly viewed, a cash management system constitutes the commingling of dividend income received from

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[2] Petitioner, like Gannett, operated a centralized cash "sweep" management system. Under Gannett's system, cash receipts are collected by operating units at the local level, deposited into their own separate bank accounts, and then "swept" to a concentration account of the parent corporation using the Automated Clearing House ("ACH") system, which is operated by the Federal Reserve. When a local operating unit needs cash for payroll or other business expenditures, the "sweep" is reversed. Such a system should be contrasted with a cash receipts and disbursements method in which all cash receipts (payments from customers) and disbursements (payments to vendors, suppliers, and personnel) are processed by a parent corporation or headquarters office using a central bank account.

subsidiaries. This Court previously held that a commingling of dividend income cannot be the test of whether a unitary business existed because that "subverts the unitary-business limitation," *F.W. Woolworth*, 458 U.S. at 364, n. 11. Likewise, when the Illinois Appellate Court relied on Petitioner's cash management system as serving an operational function it subverted the unitary business limitation.

B. Segment Reporting Serves a Financial Oversight, not Operational, Function.

In accordance with Statement of Financial Accounting Standards No. 131, *Disclosures about Segments of an Enterprise and Related Information* (1997), issued by the Financial Accounting Standards Board ("FAS 131"), all "public business enterprises" are required to report certain information about operating segments in public financial statements filed with the SEC. The objective of FAS 131 is to provide information about the different business activities in which a public company engages and the different economic environments to help users of the public company's financial statements. FAS 131 became effective for fiscal years beginning after December 15, 1997, and superseded Statement of Financial Accounting Standards No. 14, *Financial Reporting for Segments of a Business Enterprise* (1976) ("FAS 14"), and related financial accounting pronouncements. FAS 14 and related pronouncements generally required public business enterprises to report segment information by industry and geographic area.

"Operating segments are components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision

maker in deciding how to allocate resources and in assessing performance." FAS 131, at 4. When Petitioner in its public financial statements filed with the SEC reported its investment in Lexis/Nexis as a "significant business segment," that reporting was required in accordance with FAS 14 and later FAS 131 to help users of Petitioner's financial statements. Petitioner's segment reporting did not evidence any operational connection between Lexis/Nexis and Petitioner in Illinois. Indeed, if it did, then every "public business enterprise" that disposes of a reportable business segment recognizes apportionable, business income regardless of whether the underlying relationships satisfy this Court's standards under the unitary business principle, thereby effectively defeating the purposes of the unitary business principle as a limitation on the taxing authority of a State. While Petitioner clearly cared about allocating resources and assessing the performance of Lexis/Nexis, "that state of mind sheds little light on the question whether in pursuing maximum profits they treated [the stock in Lexis/Nexis] as serving, on the one hand, an investment function, or, on the other, an operational function." *Allied-Signal,* 504 U.S. at 784-785.

Petitioner's segment reporting satisfied public financial reporting requirements and served investment functions for the owners and holders of the equity and debt issued by Petitioner.

III. SINCE 19 STATES SOLELY OR SIGNIFICANTLY RELY ON THIS COURT FOR THEIR DEFINITIONS OF APPORTIONABLE, "BUSINESS INCOME," THE IMPROPER AND EXPANSIVE INTERPRETATION OF OPERATIONAL FUNCTION BY THE ILLINOIS APPELLATE COURT IS AN IMPORTANT QUESTION OF FEDERAL LAW THAT SHOULD BE SETTLED BY THIS COURT.

A total of 46 States and the District of Columbia impose a tax on the net income of corporations. Although the number of States defining apportionable, "business income" under state law using the UNIFORM DIVISION OF INCOME FOR TAX PURPOSES ACT ("UDITPA") or similar statutes[3] may maintain a slim majority, the trend among the States since this Court's decision in *Allied-Signal* is to rely solely or significantly on this Court's decisions to be their state law definitions of apportionable, business income. Thus, a number of States that used to define "business income" as a matter of state law using UDITPA now define "apportionable" or "business" income solely as "all income that is apportionable under the United States Constitution," including Illinois for transactions occurring after July 30, 2004.[4] Another group of States have retained

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[3] Under UDITPA, "business income" is defined to mean "income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations." UDITPA § 1(a). Conversely, "nonbusiness income" means "all income other than business income," UDITPA § 1(e). 7A UNIFORM LAWS ANNOTATED 141 (2005).

[4] GA. CODE ANN. § 48-7-31(a); 35 ILL. COMP. STAT. 5/1501(a)(1); MINN. STAT. § 290.17, subd. 3 and subd. 6; N.C. GEN. STAT. § 105-130.4(a)(1); and WIS. STAT. § 71.25(5)(a).

some or all of the UDITPA definition while adding "operational income" or "operationally related income" as determined under the United States Constitution to their state law definitions.[5] Of the 19 States that have broadly defined apportionable, business income, the largest group does not distinguish between "business income" and "nonbusiness income" at all. Instead, these States have chosen to treat all income as apportionable while placing the burden of proof on taxpayers to prove that particular items of income cannot be subject to apportionment based on the United States Constitution.[6] Therefore, in a minimum of 19 States the Illinois Appellate Court's decision will be at least persuasive authority in settling questions of federal law.

In *Allied-Signal* the Court provided one illustration of a capital transaction that served an operational function – interest income from short term investments that became part of a taxpayer's working capital. 504 U.S. at 787-788. Similarly, the Court provided two illustrations of transactions that did not – (1) a long-term corporate strategy of acquisitions and dispositions, and (2) use of transaction proceeds to fund future acquisitions. 504 U.S. at 788-789. The types of common capital transactions relied upon by the Illinois Appellate Court range far beyond what the

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[5] ALA. CODE § 40-27-1.1; FL. STAT. § 220.03(r); IOWA CODE § 422.32.2; N.J. STAT. ANN. § 54:10A-6.1; and 72 PA. CONS. STAT. § 7401(3)2.(1)(a).

[6] CONN. GEN. STAT. § 12-218; ME. REV. STAT. ANN. tit. 36 § 5211; MD. CODE ANN. TAX-GEN. § 10-304; MASS. GEN. LAWS ch. 63, § 38; NEB. REV. STAT. § 77-2734.06; N.H. REV. STAT. ANN. § 77-A:1; R.I. GEN. LAWS §§ 44-11-11 and 44-11-14(a); VT. STAT. ANN. tit. 32, § 5811; and VA. CODE ANN. §§ 58.1-406, 58.1-407, and 58.1-408 (dividends are allocable; all other income is apportionable).

Court illustrated in *Allied-Signal*. As more States look only to the decisions of this Court to define the income, gains, and losses they will treat as apportionable for state tax purposes, a writ of certiorari to the Illinois Appellate Court should be issued so that this Court, not the Illinois Appellate Court, can provide the proper and definitive guidance on when a capital transaction serves an operational, as opposed to an investment, function.

CONCLUSION

For the foregoing reasons, Gannett Co., Inc. respectfully requests that Petitioner's Petition for Writ of Certiorari be granted.

Respectfully submitted,

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